TEACHERS' RETIREMENT BOARD

REGULAR MEETING

SUBJECT: Update on Federal Legislation ITEM NUMBER: 10b

ATTACHMENT(S): 4

ACTION: X MEETING DATE: June 5, 2003

INFORMATION: ___ PRESENTER: Ed Derman

ELK HILLS COMPENSATION

With this year's stringent budget situation, the legislative environment for spending will be particularly difficult. The efforts to secure next year's Elk Hills compensation are complicated by the fact that the $59 million installment represents more than a 60 percent increase over the level of the previous five annual installments.

The strong letter of support signed by all 52 Members of the California Delegation in the House of Representatives has been filed with the House Interior Appropriations Subcommittee. This will be the first venue for consideration of the Elk Hills funding issue.

HOUSE WAYS AND MEANS HEARING ON SOCIAL SECURITY GPO AND WEP OFFSETS AND MANDATORY COVERAGE OF STATE AND LOCAL GOVERNMENT EMPLOYEES

On May 1, the House Ways and Means Social Security Subcommittee held a hearing regarding the Government Pension Offset and the Windfall Elimination Provision, as well as the issue of mandatory coverage, with respect to State and local government workers. A frequent comment made both by the subcommittee chair Clay Shaw and witnesses, including the General Accounting Office, is that there is an inherent link between relief from the offset provisions and the mandatory coverage of state and local employees in Social Security.

The Chair of the Teachers' Retirement Board submitted a written statement to the subcommittee expressing CalSTRS' grave concern about mandating Social Security coverage on new CalSTRS members. His statement is attached.

PORTMAN-CARDIN PENSION REFORM LEGISLATION

Representatives Rob Portman and Ben Cardin, who historically have led the bipartisan pension reform effort in the House, recently introduced H.R. 1776, the "next generation" of pension reform. Among the key provisions are:

- Acceleration in the increases in the limit on elective deferrals under Section 403(b) and Section 457 plans and annual "catch-up" contributions for participants age 50 and over;
- Favorable clarification that transfers can be made from a governmental Section 457 plan in one state to a governmental plan in another state;
- Clarification that Section 415 limits are not applicable to amounts transferred from a Section 403(b) plan or a Section 457 plan;
- Permission for plan participants to use distributions from a defined benefit or defined contribution plan, Section 403(b) plan, or Section 457 plan to fund on a pre-tax basis premiums for retiree health coverage;
- An exclusion from gross income of up to $2,000 of distributions from defined contribution or defined benefit plans, Section 403(b) plans, and Section 457 plans taken in the form of a life or joint life annuity;
- A phased increase to age 75 in the age in which minimum distributions are required;
- Direction to the Treasury to issue regulations indicating that good faith compliance by governmental plans with the minimum distribution requirement is sufficient;
- A restoration in the prior law floor on the actuarial reduction in the Section 415(b) dollar limit for retirement before age 62, with the floor being $130,000 (indexed) for retirement at age 55;
- Facilitated plan mergers between a section 403(b) plan and a defined benefit plan (or defined contribution plan); and
- Permission to contribute of up to $500 per year of the unused balance of health flexible spending accounts to a tax-qualified retirement plan.

PENSION SECURITY ACT OF 2003

The Pension Security Act of 2003 (H.R. 1000), legislation that grew out of the Enron Section 401(k) debacle, is to be considered in the full House of Representatives in May. Primarily, the legislation would amend ERISA, and thus would be of only limited concern to governmental plans such as CalSTRS. Governmental plans with self-directed investments, such as the Voluntary Investment Program, would, however, have to provide an investment education notice to participants. Other ERISA-based provisions:

- Permit a diversification of plan investments by the participant after certain periods of participation;
- Provide for fiduciary liability during "blackout" periods when participants are barred from accessing their accounts;

- Permit investment advice to be offered to plan participants by investment advisors to the plan; and
- Create a new tax deduction for retirement planning expenses of a participant.

PROTECTION OF PENSION ASSETS FROM BANKRUPTCY OF PARTICIPANT AND EMPLOYER

The full House has passed bankruptcy reform legislation (H.R. 975) that includes helpful provisions to protect the interests of plan participants when either they or their employer file for bankruptcy. Its prospects in the Senate are uncertain.

IMPLEMENTATION OF THE SARBANES-OXLEY CORPORATE GOVERNANCE AND ACCOUNTING REFORM LEGISLATION BY THE SEC AND THE PCAOB

CalSTRS federal counsel continues to provide CalSTRS staff with regular written updates on the implementation by the Securities and Exchange Commission of various major components of the Sarbanes-Oxley corporate governance and accounting reform legislation.

William McDonough, the former President of the New York Fed, has been appointed as Chairman for the new Public Company Accounting Oversight Board (PCAOB). The PCAOB continues to hire staff and to ramp up its operation to begin its registration and oversight of accounting firms that audit public companies and has approved a budget of $68 million for this year. The new Board also must establish standards for auditing, internal controls, and auditor ethics and independence.

Attached is the official text of new PCAOB Chairman William McDonough's recent letter to the Chairman and CEO of Morgan Stanley in response to the latter's remarks following the recent settlement regarding abuses in analyst research.

SUMMARY OF FEDERAL LEGISLATION

Mr. Derman will provide a verbal update at the meeting.